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In the Supreme Court of the United States

OCTOBER TERM, 1939

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

PAUL R. G. HORST

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above-entitled cause on December 2, 1939, reversing the decision of the United States Board of Tax Appeals.

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 24) is reported in 39 B. T. A. 757. The opinion of the Circuit Court of Appeals (R. 46) is reported in 107 F. (2d) 906.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 2, 1939 (R. 49). The

jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the owner of coupon bonds should include in his gross income the amount of coupons which he detached and gave to his son several months prior to maturity.

STATUTE INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived * * * from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * [U. S. C., Title 26, Sec. 22].

STATEMENT

The stipulation of facts (R. 39–43) was adopted by the Board of Tax Appeals as its findings of fact; they are substantially as follows (R. 25–26):

Taxpayer is and was during the years 1934 and 1935 a citizen of the United States, temporarily residing in Paris, France (R. 25).

During the years 1934 and 1935 taxpayer kept his books and made his income-tax returns on the cash receipts and disbursements basis (R. 25).

Throughout the year 1934 taxpayer owned foreign, state, municipal, and industrial coupon bonds. On August 10, 1934, he detached, prior to their maturity, negotiable interest coupons and transferred them by manual delivery to his son, Robert P. K. Horst, as a gift. They had an aggregate face value of $25,182.50. (R. 25.) All of the coupons matured during the year 1934; and in that year the son collected the total amount due and reported it in his income-tax return for that year (R. 25).

Throughout the year 1935 taxpayer owned foreign, state, municipal, and industrial coupon bonds. In August 1935 he detached, prior to their maturity, negotiable interest coupons and transferred them by manual delivery to his son as a gift. They had an aggregate face value of $37,032.50. (R. 25.) All of the coupons matured during the year 1935, and in that year the son collected the amount of $25,495 and reported it in his income-tax return for that year (R. 26).

The taxpayer did not report in his income-tax returns for the years 1934 and 1935 any part of the amount represented by the interest coupons delivered as a gift to his son in those years (R. 26). The Commissioner in determining the deficiency for the year 1934 added to the taxable income of the taxpayer the amount of $25,182.50 as the value of the coupons transferred to his son in that year, and in determining the deficiency for the year 1935 the Commissioner added to the taxable

income of the taxpayer the amount of $22,360 as the aggregate net worth of all of the coupons transferred by taxpayer to his son in that year (R. 26). The deficiency in income tax for the year 1934 resulted solely from the addition to income of the ~~value as set here. (R. 26.)~~ transferred coupons. The deficiency for the year 1935 resulted from the addition to income of the value of the transferred coupons plus certain other minor adjustments not in controversy here (R. 26).

The Board of Tax Appeals upheld the Commissioner's determination, with three members dissenting, and the taxpayer appealed to the Circuit Court of Appeals, which reversed the Board's decision and held that the amount of the coupons was not income of the taxpayer.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the owner of bonds need not include the amount of certain coupons in his gross income where he detached and gave the coupons to his son several months prior to maturity.

2. In failing to hold that the owner of bonds should include the amount of certain coupons in his gross income although he detached and gave the coupons to his son several months prior to maturity.

3. In reversing the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below conflicts in principle with decisions of this Court and of the circuit courts of appeals.

In *Helvering* v. *Clifford,* No. 383, this Term, decided February 26, 1940, this Court held the grantor of an irrevocable but short term trust taxable upon the income payable to the beneficiary. The issue, the Court said, was simply "whether the grantor after the trust has been established may still be treated, under this statutory scheme, as the owner of the corpus" (p. 3). The short period before reversion, and the retention of control over the principal, fortified by the familial relations between settlor and beneficiary, provided the solution to that issue. The result in the present case should follow *a fortiori* from the *Clifford* decision. For here the taxpayer has surrendered simply his claim to future income and has retained intact the entire bundle of rights which constitute his ownership of the underlying property.[1]

The decision below is not only in conflict with the *Clifford* case, but the court below has ignored the settled rule relating to the assignor's taxability upon assigned future income. *Lucas* v. *Earl,* 281 U. S. 111, in which the rule was first established,

[1] There can be no question that the coupons represented interest, divorced from the principal. *Old Colony R. Co.* v. *Commissioner,* 284 U. S. 552, 561; see *Deputy* v. *duPont,* No. 151, this Term, decided January 8, 1940.

dealt, it is true, with the income from personal services. But the basis of the decision is the broad principle that tax liability remains the same whether the income is assigned before or after its receipt; in this doctrine there is no room for distinction according as the future income is derived from the taxpayer's services or his ownership. Thus, in *Burnet* v. *Leininger,* 285 U. S. 136, the assignor was held taxable when the income, derived from a laundry partnership, was produced by a combination of property and personal services. And in *Reinecke* v. *Smith,* 289 U. S. 172, 177, the Court noted that "This court has repeatedly said that such an assignment, where the assignor continued to own the corpus, does not immunize him from taxation upon the income." See also *Saenger* v. *Commissioner,* 69 F. (2d) 631, 632 (C. C. A. 5th). With minor exceptions,[2] the circuit courts of appeals have consistently held that unless the taxpayer assigns the corpus which produces the income, he cannot by assignment of future income be relieved of taxation on that income. *Bing* v.

[2] In *Rosenwald* v. *Commissioner*, 33 F. (2d) 423, certiorari denied, 280 U. S. 599, the amount of income in dispute was about $830,000, of which about $815,000 represented assigned income from rents, stocks, and bonds, while $15,000 represented income from bond coupons assigned by the owner of the bonds. The court held the owner taxable on all except the coupons. The Government did not apply for a writ of certiorari in regard to the assigned coupons because of the relatively small amount of tax involved. Cf. *Matchette* v. *Helvering*, 81 F. (2d) 73 (C. C. A. 2d), certiorari denied, 298 U. S. 677.

Bowers, 22 F. (2d) 450, 454 (S. D. N. Y.) affirmed, 26 F. (2d) 1017 (C. C. A. 2d); *Rosenwald* v. *Commissioner,* 33 F. (2d) 423, 426 (C. C. A. 7th), certiorari denied, 280 U. S. 599; *Porter* v. *United States,* 52 F. (2d) 1056 (C. Cls.); *Ward* v. *Commissioner,* 58 F. (2d) 757 (C. C. A. 9th), certiorari denied, 287 U. S. 656; *Dickey* v. *Burnet,* 56 F. (2d) 917, 921 (C. C. A. 8th), certiorari denied, 287 U. S. 606; *Wood* v. *Commissioner,* 74 F. (2d) 78 (C. C. A. 6th).[3]

The substance of the transaction is, in truth, simply a gift by respondent of his income to his son. He clearly would be taxable on the amount of the bond coupons if he had collected the interest payments before giving the proceeds to his son; or, indeed, if he had directed the son to collect the coupons as his agent and to keep the proceeds as a gift.[4] These technical variations upon the transaction would not alter its practical substance, and respondent is taxable in this case equally with its

[3] See also 2 Paul & Mertens, *Law of Federal Income Taxation* (1934), Sec. 15.03, p. 25. A case substantially similar to this is now pending decision in the Supreme Judicial Court of Massachusetts. *Williston* v. *Commissioner of Corporations and Taxation,* Nos. 9063–9064.

[4] Indeed, under ordinary standards, the respondent made a gift to his son which was largely past rather than future income. The coupons were given one to four months in advance of maturity (R. 5, 16, 40, 42). Although respondent kept his books upon a cash basis, the commercial truth of the matter is that the accrued interest was already his; he could have discounted the coupon or, had he sold the bond, his receipts would have included the accrued interest.

variations. See *Griffiths* v. *Helvering,* No. 49, this Term, decided December 18, 1939; *Higgins* v. *Smith,* No. 146, this Term, decided January 8, 1940.

2. The question is one of considerable importance. The substantial conflict in decisions will inevitably result in confusion in the lower courts. And should the result below become accepted, taxpayers have obtained a ready means by which to escape the surtax rates without surrendering control of their propety.[5]

CONCLUSION

It is therefore respectfully submitted that this petition for a writ of certiorari should be granted.

FRANCIS BIDDLE,
Solicitor General.

MARCH 1940.

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[5] Tax services have already pointed out that the decision of the court below may be used to advantage by taxpayers. 1939 C. C. H., Vol. 1, pp. 461, 463; Alexander Tax News Letter, Vol. IV, No. 19, November 24, 1939. While it is true that there would be a gift tax on gifts of bond coupons amounting to more than $4,000, the gift tax would not reach gifts of less than that amount, and the donee in practically all cases would be in a lower surtax bracket than the donor.

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